(3)

Office - Supreme Court, U. S.
FILED
NOV 7 1941
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 696

In the Matter

of

GODFREY-KEELER CO., INC., Debtor,

Petitioner,

—against—

THE WICKES BOILER COMPANY, INC.,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

ALFRED B. NATHAN,
Counsel for Respondent.

THE COURT PRESS, N. Y. C.

INDEX.

PAGE

Statement 1

Point I—There is no ground for granting certiorari.. 3

Point II—Petitioner's contentions on the merits.... 7

Petitioner's Contention That the Trust Provisions of Section 36-a of the New York Lien Law Protect Only Those Sub-contractors Who Have Filed Liens 8

Petitioner's Contention That Its Filing of a Petition of Arrangement Prior to Its Receipt of the Money from the Owner, Renders Section 36-a of the Lien Law Inoperative 11

Petitioner's Contention That Section 36-a of the New York Lien Law Creates an Unauthorized Priority in Contravention of Section 64 of the Bankruptcy Act 14

Conclusion 15

Table of Cases Cited:

Amiesite Construction Corp. v. *Luciano Contracting*, 284 N. Y. 223..... 12

Boise v. *Talcott*, 264 Fed. 61 (C. C. A. 2)..... 11

Club Holding Co. v. *Flint Citizens' Loan & Investment Co.*, 272 Mich. 66, 261 N. W. 133..... 4

Edward Misch Co.'s Estate, 112 Fed. (2) 1007, aff'g 34 Fed. Supp. 781 (6th Circuit).....4, 5, 6

Fox & Co. v. *State*, 229 Wisc. 44, 281 N. W. 666..... 10

PAGE

Horton v. *Queens Co. Machinery Corp., Inc.*, 101 Misc. 31 13

Huntington v. *Attrill*, 146 U. S. 657..... 5

Murphy v. *National Paving Co.*, 229 Wisc. 100, 281 N. W. 705..... 10

New York Trap Rock Corp. v. *National Bank of Far Rockaway*, 285 N. Y. 313..... 8, 9

Pauly v. *Keebler*, 175 Misc. 428..... 10

Raymond Concrete Pile Co. v. *Federation Bank & Trust Co.*, 262 App. Div. 847..... 9

Raymond Concrete Pile Co. v. *Federation Bank & Trust Co.*, 261 App. Div. 25..... 8, 9

Ruhlin v. *New York Life Insurance Co.*, 304 U. S. 202. 4

York Trim Corp. v. *Ardley Trading Corp.*, 169 Misc. 656 8

OTHER AUTHORITIES CITED:

Bankruptcy Act:
Section 75 (1910 Amendment)..... 13
Section 64..... 14

Judicial Code, Section 240, Subdivision a..... 3

Lien Law of the State of New York:
Section 36-a 1, 2, 3, 4, 7, 8, 10, 11, 12, 14
Sections 36-c, 36-d and 36-e..... 7
Section 25-a.....9, 12

Michigan Public Acts of 1931, Act 259..... 4

New York Personal Property Law, Section 65..... 13

Reports of the New York Joint Legislative Committee 8

IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No.

In the Matter

of

GODFREY-KEELER CO., INC., Debtor,

Petitioner,

—against—

THE WICKES BOILER COMPANY, INC.,

Respondent,

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Statement.

This is an application for a writ of certiorari to the Circuit Court of Appeals for the Second Circuit. The Circuit Court decision of which petitioner complains, affirmed a decision of the District Court for the Southern District of New York, which in turn affirmed a decision of Hon. Irwin Kurtz, Referee in Bankruptcy.

The proceeding before the Referee was brought by The Wickes Boiler Company, Inc. under Section 36-a

of the Lien Law of the State of New York. Section 36-a provides as follows:

> "Sec. 36-a. Contractor who diverts funds guilty of larceny.
>
> The funds received by a contractor from an owner for the improvement of real property are hereby declared to constitute trust funds in the hands of such contractor to be applied first to the payment of claims of subcontractors, architects, engineers, surveyors, laborers and materialmen arising out of the improvement, and to the payment of premiums on surety bond or bonds filed and premiums on insurance accruing during the making of the improvement and any contractor and any officer, director or agent of any contractor who applies or consents to the application of such funds for any other purpose and fails to pay the claims hereinbefore mentioned is guilty of larceny and punishable as provided in section thirteen hundred and two of the penal law. Added L. 1930, c. 859, Sec. 18, eff. Oct. 1, 1930."

The petitioner Godfrey-Keeler Co., Inc. had installed a power plant and heating system in the premises of the Brooklyn Yarn Dye Company, at 24 Woodward Avenue, Brooklyn, New York (fols. 10, 60). The respondent, The Wickes Boiler Company, Inc. under a contract with the petitioner, had furnished the boilers for said power plant and heating system (fols. 11, 60). Godfrey-Keeler Co. Inc. then filed a petition for arrangement. At the time of the filing of the petition there remained due from Brooklyn Yarn Dye Company to petitioner on the principal contract a balance of about $8800 (fols. 12, 61-62),

and at that time there remained due from petitioner to respondent for its boilers a balance of $1,810.50 (fols. 12, 60).

Godfrey-Keeler Co. Inc., without paying the claim of The Wickes Boiler Company, Inc. and the other sub-contractors, laborers and materialmen on the Brooklyn Yarn Dye Company job, proposed to use the money to be received from the Brooklyn Yarn Dye Company to consummate its proposed arrangement with the general creditors (fols. 17, 18). To prevent this and to enforce the trust created by Section 36-a of the Lien Law, The Wickes Boiler Company, Inc. made an application before the Referee to impress a trust on the moneys due from the Brooklyn Yarn Dye Company. The application was granted and, as we have already pointed out, the Referee's decision has been sustained by the District Court and the Circuit Court. (To avoid confusion, we point out that in the proceeding before the Referee, The Wickes Boiler Company, Inc. was the petitioner, and is so referred to in the record. On the present application for a writ of certiorari, the Godfrey-Keeler Co. Inc. is, of course, the petitioner, and The Wickes Boiler Company, Inc. the respondent.)

POINT I.

There is no ground for granting certiorari.

The jurisdiction of this court is invoked under Subdivision (a) of Section 240 of the Judicial Code (Pet., p. 2). The sole reason urged by petitioner for the granting of the writ is an alleged conflict between the Circuit Courts for the Second and Sixth Circuits (Pet., p. 5).

There is no such conflict between the Circuits as warrants the granting of this application. Both Circuit Courts merely applied state law, and as to questions controlled by state law, a conflict among Circuits is not of itself a reason for granting a writ of certiorari.

Ruhlin v. *New York Life Insurance Co.*, 304 U. S. 202.

The principal case involved the construction and effect of Section 36-a of the Lien Law of the State of New York. The case of *Edward Misch Co.'s Estate*, 112 Fed. (2) 1007, aff'g 34 Fed. Supp. 781, in the Sixth Circuit, involved the construction and effect of Act 259 of Michigan Public Acts of 1931.

As petitioner itself recognizes (Pet.'s Brief, bottom of p. 11), the courts of New York give effect to Section 36-a as a civil statute creating substantive rights enforceable by the subcontractors and other beneficiaries named in the section. The Supreme Court of Michigan, on the other hand, has held that Act 259 of Michigan Public Acts of 1931 is purely a criminal statute and does not create substantive civil rights which the subcontractors and other beneficiaries of the trust can enforce. (*Club Holding Co.* v. *Flint Citizens' Loan & Investment Co.*, 272 Mich. 66, 261 N. W. 133.)

The Federal Courts in the Second Circuit applied the law of New York in determining the construction and effect to be given to Section 36-a of the Lien Law of the State of New York, and the Federal Courts in the Sixth Circuit applied the Michigan law in determining the construction and effect to be given to Act 259 of Michgan Public Acts of 1931. Surely, it

is not the province of this court to tell the Legislatures of New York and Michigan what statutes to enact, nor to direct the courts of New York and Michigan as to the interpretation to be given to the statutes of their respective states.

Petitioner seeks to persuade this Court that the federal courts in the principal case and in the *Edward Misch Co.* case were not applying state law. Then what law were they applying? Is it seriously contended that there is a body of federal law governing the interpretation of the Lien Statutes of New York and Michigan?

Petitioner relies on *Huntington* v. *Attrill*, 146 U. S. 657, which has no application whatever. In that case it was sought to enforce a New York statute in a Maryland court, and it was contended that the Maryland court did not have to enforce the statute because that would be giving effect to the Penal Law of another state. This court pointed out that the question presented was "whether this statute is a Penal Law in the international sense" (p. 679). In other words, the Maryland court was required to determine whether, under the rules of international law, it should take jurisdiction of the case. Such a question might have been determinable by the law of the forum. But even then, the law of the forum would apply only to the jurisdictional question. Once the court determined to take jurisdiction, its decision as to the construction and effect of the statute would be governed by the law of the enacting state.

Of course, no question of jurisdiction or international law was presented either in the principal case or in the *Misch Co.* case. The Wickes Boiler Company in the principal case and the R. C. Mahon

Company in the *Edward Misch Co.* case applied to the federal courts for the purpose of having trusts imposed on certain moneys coming into the hands of trustees in bankruptcy. The relief sought was purely civil. The criminal aspects of the statutes were not involved at all, and these were not cases of courts being asked to enforce the Penal Laws of foreign jurisdictions.

The question whether the statutes were purely penal or whether they also created substantive rights, was considered solely for the purpose of determining the merits of the controversy, viz., whether the petitioning subcontractors had enforcible claims as trust beneficiaries. The question was entirely one of statutory construction determinable by state law. As the District Court pointed out in the *Edward Misch Co.* case:

> "It appears to this Court that the construction placed upon the statute in question by the Michigan Supreme Court in the case of *Club Holding Company* v. *Flint Citizens' Loan & Investment Company* reported in 272 Mich. 66, 261 N. W. 133 is conclusive upon the question. In passing upon a State statute, this Court is constrained to give effect to the same in harmony with the decisions of the court of last resort of such state."

The Circuit Court of Appeals for the Sixth District affirmed "upon the ground and for the reasons stated in the opinion of the District Judge * * *."

We have thus far assumed that there is a conflict between the decisions in New York and the decisions in Michigan. Actually, the statutes of the two states

are quite dissimilar. The sections which immediately follow Section 36-a of the New York Lien Law make it perfectly plain that the New York statute was intended to confer substantive civil rights which the beneficiaries of the trust could enforce (Secs. 36-c, 36-d and 36-e of the Lien Law of the State of New York).

POINT II.

Petitioner's contentions on the merits.

Petitioner's arguments on the merits serve to emphasize that the Federal Courts in the Second and Sixth Circuits were merely applying state law, and that if there is any conflict at all, it is a conflict between the Lien Law of New York and the Lien Law of Michigan. Accordingly, petitioner has shown no ground for granting the writ.

Since petitioner has nevertheless, seen fit to submit a brief on the merits, we shall take the liberty of discussing certain of the points involved in the case. These have already been discussed at some length in the opinions of the Circuit Court (fols. 121-140, 170-180), the District Court (fols. 88-93), and the Referee (fols. 59-75), and we shall confine ourselves to very brief comment on certain of the contentions advanced in petitioner's brief.

Petitioner's Contention That the Trust Provisions of Section 36-a of the New York Lien Law Protect Only Those Sub-contractors Who Have Filed Liens.

Before the Referee and in the District Court petitioner argued that the Wickes Boiler Company, Inc. was not entitled to enforce the trust created by Section 36-a because it had not filed a notice of lien. On the original argument of the appeal in the Circuit Court, however, petitioner made no contention whatsoever based upon the fact that respondent had not filed a notice of lien. Accordingly, it was not until the reargument that this point was briefed by counsel and fully considered by the court.

Petitioner, at page 15 of its brief, makes an inaccurate and misleading statement as to the grounds for the Circuit Court's decision on this point. As we shall show presently, the refusal of the Court of Appeals in *New York Trap Rock Corp.* v. *National Bank of Far Rockaway,* 285 N. Y. 313, to approve the Appellate Division, 2nd Dept.'s, construction of the statute would have been sufficient ground for the Circuit Court's decision on the reargument. But the Circuit Court did not rely on that alone. It also relied on the decision of the Appellate Division, First Dept., in *Raymond Concrete Pile Co.* v. *Federation Bank & Trust Co.,* 261 App. Div. 25, and upon the express language of Section 36-a and the reports of the New York Joint Legislative Committee (fols. 175-179). It was perfectly apparent that the decision of the Appellate Division, Second Department, was an isolated departure from the generally accepted rule, and that it did not represent the law of New York (see, for example, *York Trim Corp.* v. *Ardley Trading Corp.,* 169 Misc. 656).

We might add that after the Second Department decision in *N. Y. Trap Rock Corporation* v. *National Bank of Far Rockaway* (*supra*), a motion for reargument was made to the Appellate Division, First Dept., in the *Raymond Concrete Pile* case, in reliance upon the Second Dept. decision. The Appellate Division, First Dept., denied the motion (*Raymond Concrete Pile Co.* v. *Federation Bank & Trust Co.*, 262 App. Div. 847).

But getting back to the Court of Appeals decision in the *N. Y. Trap Rock* case, there is a strong indication in the decision itself that the Court of Appeals disagreed with the Appellate Division's construction of the section in question. The Court of Appeals' affirmance was based on a procedural ground which the Appellate Division had not even mentioned in its decision. The effect of this procedural affirmance was to dismiss the complaint and to require the plaintiff to start a new action—this time in equity, rather than at law. It is difficult to believe that the Court of Appeals would have required the plaintiff to make this procedural change in the form of his action, if it had agreed with the Appellate Division that the plaintiff had no cause of action at all. Had it agreed with the Appellate Division on the substantive ground, the Court of Appeals certainly would have disposed of the case on that ground. It would not have required the plaintiff to correct a procedural defect, before throwing him out on the merits. Incidentally, the Court of Appeals decision to the effect that the construction of Section 25-a was not necessarily presented in the *New York Trap Rock* case, would seem to render the decision of the Appellate Division in that case nothing more than dictum.

Petitioner cites *Pauly* v. *Keebler,* 175 Misc. 428 (Petitioner's Brief, pp. 15-16). The statute construed in that case was expressly limited in its application "to persons entitled to a lien under this chapter * * *". The difference between such a statute and Section 36-a of the Lien Law requires little comment. The New York Statute contains no such limitation as the statute just referred to. In fact, as the Circuit Court points out, the New York Statute expressly covers certain persons who are not even permitted to file liens (fols. 177-179).

Petitioner neglects to mention the more resent Wisconsin case of *Murphy* v. *National Paving Co.,* 229 Wisc. 100, 281 N. W. 705. That case involved a statute which did not contain the restrictive language of the earlier statute, and it was there held that a sub-contractor could enforce the trust, even though he had not acquired a lien. Petitioner also neglects to mention the Wisconsin case of *Fox & Co.* v. *State,* 229 Wisc. 44, 281 N. W. 666, in which the court pointed out, at page 49:

> "The term 'claim' [which is the term used in both the N. Y. and Wisconsin trust statutes] is more comprehensive than 'lien' and includes nonlienable items, so long as they are germane to performing such contract upon the public work. The legislature evidently intended that the rights of those contributing their labor or materials to the public work should be protected above other creditors whose claims bear no relation to the public improvement."

Petitioner's Contention That Its Filing of a Petition of Arrangement Prior to Its Receipt of the Money from the Owner, Renders Section 36-a of the Lien Law Inoperative.

The proposition that a trustee in bankruptcy will not be bound by the rights and obligations which a statute creates unless the statute makes express reference to such trustee in bankruptcy, is indeed a novel one. It is only by virtue of his status as trustee, that the trustee in bankruptcy receives the money at all. He receives the money subject to the same trust which would be imposed against the bankrupt.

At the time of the filing of the petition for arrangement, the bankrupt had no absolute right to the money. All that the trustee inherits from the bankrupt is the bankrupt's right to receive the money as trustee. That is all the bankrupt had, and that is all the trustee gets. As Judge Leibell pointed out in his decision (fol. 90):

> "The filing of the petition under Ch. XI could not enlarge or clear the debtor's title to these funds."

The concept is elementary and is well stated in *Boise* v. *Talcott* (C. C. A. 2), 264 Fed. 61, as follows:

> "A trustee in bankruptcy takes the property of the bankrupt, not as an innocent purchaser, but as the debtor had it at the time of the petition, subject to all valid claims, liens and equities. *Zartman* v. *First National Bank,* 216 U. S. 134."

Clear it is therefore that the trustee cannot take the money and at the same time repudiate the bank-

rupt's obligation to receive that money as trustee. There is nothing in the language of Section 36-a itself which justifies any such result. It is difficult to see how the Legislature could have used very different language. It was imposing a trust and providing criminal penalties for the violation of that trust. The Legislature couldn't very well impose this trust obligation on the contractor until the money came into his hands. Naturally enough, therefore, the section says that "The funds received by a contractor" shall constitute trust funds "in the hands of such contractor". But it is nothing short of absurd to try to torture this perfectly natural language into an expression of intention to sweep aside the fundamental principles of bankruptcy law and to confer upon a trustee in bankruptcy a better title than that possessed by his bankrupt.

Petitioner refers to *Amicsite Construction Corp.* v. *Luciano Contracting,* 284 N. Y. 223. In that case the money was not in the hands of the contractor because it had not yet been paid to him and was still in the hands of the state. And that is what the court meant when it pointed out that Section 25-a had no application because the money was not "in the hands of the contractor". The court was not drawing any distinction between a contractor and his trustee in bankruptcy.

In an effort to show that a trustee in bankruptcy can sometimes get better rights than the bankrupt would have, petitioner at page 14 of its brief refers to the case of a conditional vendor who has failed to file a copy of his contract, as required by law. In such a case the contract, although valid as between the original parties, is held void as against a trustee

in bankruptcy. However, this result is based entirely upon Section 65 of the New York Personal Property Law, which expressly provides that an unfiled conditional sales contract shall be void as against the creditors of the conditional vendee.

Petitioner points out at pages 14-15 of its brief that the Bankruptcy Act gives a trustee in bankruptcy the rights of an attaching or judgment creditor. Petitioner is here referring to the 1910 amendment to Section 75 of the Bankruptcy Act. It is elementary that the sole purpose and effect of this amendment is to place the trustee in a position to attack unlawful transfers made by the bankrupt. As pointed out in *Horton* v. *Queens Co. Machinery Corp. Inc.,* 101 Misc. 31, at page 35:

> "This section [Sec. 75, formerly Sec. 47] does not deal with the title of the trustee to the bankrupt's property, but only with the trustee's duties. The provisions relating to title are contained in Sec. 70. The provisions of the amendment in question plainly deal only with the question of remedy or procedure. The reason for the adoption of this amendment and the objections sought to be accomplished by it are generally agreed to both by text writers and decisions. These are said to be to overcome the effect of the decisions like *York Mfg. Co.* v. *Cassell,* 201 U. S. 344; *Matter of N. Y. Economy Printing Co.,* 110 Fed. 514, and to enable the trustee to attack secret liens created or transfers made by bankrupts which otherwise could not be attacked. Collier on Bankruptcy, 9th Ed. (659-661)."

Petitioner's Contention That Section 36-a of the New York Lien Law Creates an Unauthorized Priority In Contravention of Section 64 of the Bankruptcy Act.

Petitioner asserts that respondent is claiming a "priority" and that Section 64 of the Bankruptcy Act recognizes only priorities created by United States Law and not priorities created by state law. If the argument is sound, then no trusts whatsoever would be recognized by the Bankruptcy Courts. Trusts are created either by agreement between the parties or by state law. They are not generally created by United States law.

Turning over trust money to the *cestui* of a trust is not the payment of a debt of a bankrupt estate, and Section 64 of the Bankruptcy Act relating to priorities has no application. The question of priorities can be involved only where unsecured creditors are claiming payment out of the general fund in the hands of the trustee. Trust funds aren't part of the bankrupt estate and the *cestui's* claim to the trust money is not the assertion of a priority under Section 64 of the Bankruptcy Act.

Petitioner suggests the possibility that state legislatures might create trusts in all kinds of situations to the prejudice of general creditors. Entirely apart from the constitutional prohibitions against the arbitrary creation of trusts, petitioner's argument is beside the point and should be addressed to Congress. A trust and a priority are two entirely different things, and the Bankruptcy Act as it now stands gives effect to trusts whether created by indenture or by State statute. Indeed, there would be serious question as to the power of Congress to refuse to give effect to trusts created by valid state statutes.

CONCLUSION.

There is no such conflict between the Circuit Courts for the Second and Sixth Circuits as warrants the granting of a writ of certiorari, and the application should be denied.

Respectfully submitted,

ALFRED B. NATHAN,
Counsel for Respondent.